Value for money assessments: Taking it step by step

Rita Butler-Jones provides a four-step checklist to help DC schemes carrying out value for money assessments

From 31 December 2021, new regulations come into force that require DC schemes to carry out extended value for money assessments and report back on whether consolidation into another scheme would improve outcomes for their members.

These new reporting obligations will initially only affect DC schemes with assets of less than £100 million. However, a consultation is underway to consider whether the regulations should be extended to schemes with assets of between £100 million and £5 billion.

Meanwhile, from 1 October, increased investment reporting requirements were introduced that apply to all schemes.

To help support you, we've put together our four-step checklist, which offers you useful tips and guidelines for addressing the new changes affecting pension consolidation.

Step 1 – Familiarise yourself with the legislation changes

Trustees of in-scope schemes must carry out a holistic assessment of how their scheme delivers value for members. The outcome of this assessment must be reported in the annual chair's statement and include consideration of reported costs and charges, fund performance (investment returns) and other measures of scheme governance and administration.

Since 1 October 2021, further regulations have taken effect (for the first scheme year ending after that date) where trustees of all schemes will be required to report their net investment returns.

As a minimum, returns from April 2015 (or the start date of the scheme if later) should be reported. The regulations specifically refer to costs and charges 'relating to those investments', so separate administration charges could be excluded.

Step 2 – Carry out the tasks listed in this summary trustees of in-scope schemes will need, in sum, to assess and report on:

• costs and charges – comparing the charges of the scheme and funds against alternative schemes

• the way you report on net investment returns

• measures of governance and administration – providing a self-assessment of record-keeping and member communications

• whether members are receiving value for money, and if not, whether to consolidate

Your findings should be reported as part of the chair's statement and annual scheme return.

Step 3 – See the following overview on how to comply with the requirements

Costs, charges and net returns:

• Trustees will need to compare costs, charges and net returns against three other larger schemes which have assets of greater than £100 million. This could be another own trust scheme, a master trust or a contract-based arrangement. This applies to all default arrangements and self-select funds. Of the three larger schemes chosen, the trustees should have discussed a potential transfer with at least one of those schemes, should they decide to wind up and consolidate

• Default funds should be compared with the default of the comparator, even if the comparator has a different investment strategy

• Self-select funds should be compared to the 'nearest comparable funds'. If the comparator scheme does not offer comparable funds such as legacy or with profits, the trustees should compare against the default

• However, trustees are expected to give more weight to net returns and their ability to properly manage the scheme than solely focusing on charges

Governance and administration:

• Trustees must carry out a self-assessment of their governance and administration, following the approach set out in the Department for Work and Pensions guidance and The Pensions Regulator's (TPR) DC Code of Practice, including:

• promptness and accuracy of financial transactions

• quality of record-keeping

• appropriateness of the default strategy

• quality of investment governance

• level of trustee knowledge, understanding and skills to run the scheme effectively

• quality of communications with members

Assessing whether members receive value for money:

• Taking all the above aspects into account, the trustees need to decide whether members receive good value

• If the scheme is deemed not to

provide value for members overall, trustees are expected to consider winding up and consolidating

• If trustees do not take immediate action to wind up, they must explain why and set out what steps they will take to ensure the scheme delivers value

• The impact of wind-up costs should be considered but needs to be weighed against the benefits of moving to a better-governed scheme with lower costs and potentially higher long-term net returns even if wind-up costs are very high

• If trustees strongly believe that only small areas of improvement are required and the resource and cost commitment is more favourable than winding up, that option can be explored but only if the proposed improvements are sustainable in the long term

Reporting:

• The outcome and explanation of the assessment should be reported in the chair's statement. The outcome should also be reported in the annual TPR scheme return alongside actions that will be taken

Step 4 – Check to see whether Legal & General can help

We're well-placed with the knowledge, expertise and resources to support you in meeting the new legislative obligations and in improving outcomes for members. So, why not get in touch with us to see if we can help?

We already support clients with information on costs, charges and net investment returns. If your scheme is administered by Legal & General, we can also provide guidance on measuring levels of achievement in administration, such as checking performance against service standards and record-keeping scores.

In addition, as the provider of the largest commercial master trust in the UK and with over £16 billion* of assets, we can further support in-scope schemes by:

• providing a comparison of costs, charges and net returns for the L&G Mastertrust's default and self-select funds

• discussing with you any potential decision to wind up and consolidate

• offering you the reassurance of knowing that the L&G Mastertrust is run by trustees who are legally responsible for making sure that the costs and charges give good value for money, and who act on behalf of members to regularly assess the trust's costs against a series of measures. Our independent trustees work hard with Legal & General to make sure that all charges are fair and competitive

• passing on the benefits of the economy of scale that comes from being the largest pension provider in the UK, with over £130 billion* of assets and four million members

• having a clear and compelling set of financial ambitions that deliver income and growth

• being committed to delivering profitable growth and to investing in society's future

If you'd like to find out more, please visit www.lgim.com/scheme-consolidation

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